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No. 74-1407

In the
Supreme Court of the United States
October Term, 1974

RODMAN & RENSHAW,
Petitioner,

vs.

ROBERT AND SANDRA SCHAEFER, et al.,
Respondents.

OPPOSITION TO PETITION OF RODMAN AND RENSHAW FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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Respondents, Robert and Sandra Schaefer, et al., and members of the class they represent, oppose the petition of Rodman & Renshaw, for a writ of certiorari to review the decision and judgment of the court of appeals for the Seventh Circuit of January 30, 1975 on the issues presented by petitioner. Respondents in this petition have filed their own petition to review another distinct and separate part of said decision of that court under No. 74-1366.

QUESTIONS PRESENTED

Respondents cannot, for the most part, accept the delineation of issues in the petition as presented by petitioner, Rodman & Renshaw (Rodman).

(1) Rodman states the first and primary issue in their petition as

> 1. Whether a cause of action for damages for manipulation of prices of shares of stock listed on a national exchange for which a specific damage remedy is available under § 9 of the Securities Exchange Act of 1934 may also be implied under §10 (b) of that Act and Rule 10(b)(5) of the Securities Commission *where the action would be time barred by the limitations period of §9(e) of the Act?* (emphasis supplied by respondents)

Referring to the emphasized portion, there is nothing in the record of this case through the court of appeals to indicate if respondents' claims based on the stock manipulation were denied under Section 10 (b), Rule 10B-5 of the 1934 act and restricted to Section 9 that the claim against Rodman would be *ipso facto* time barred by the Section 9(e) limitations. The rulings in the district court and most recently in the Seventh Circuit have consistently upheld respondents' claim under Section 10(b). Accordingly, the application of the Section 9 limitations period to any of the alleged manipulation conspiracy defendants has never been decided and hardly argued. A fair statement of the Question No. 1 as presented in Rodman's petition would therefore be as follows:

> 1. Whether a claim for relief based on an alleged fraudulent manipulation of a security on a national securities exchange may be brought by purchasers under Section 10(b), Rule 10B-5 as well as under Section 9?

(2) Rodman's petition states the second question as:

> 2. Whether any private right of action for damages may be implied under § 17 of the Securities Act of 1933 and whether if such a right is implied, a privity requirement exists as a predicate to its maintenance?

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Respondents do not contest the wording of this question in the abstract but state that this question was not part of the decision and judgment of the Seventh Circuit and therefore is nothing for this court to review.

Accordingly, Rodman's Question No. 2 ought to be eliminated.

(3) Rodman's petition states the third question as follows:

> 3. Whether, if the limitations period of the forum state is to be applied, the period should be tolled as to defendant *whose liability is derivative and vicarious and is not predicated upon complicity in the fraudulent scheme but upon negligence facilitating the fraud?* (emphasis supplied by respondents)

This statement of Question No. 3 is erroneous because it mis-states the primary basis of respondents' claim against the brokerage firm, Rodman & Renshaw. The emphasized portion assumes that the claim is based primarily on fraud through the conduct of employe and customer's representative, Harris Nagorsky and principals of the firm.

There is therefore no issue in the record of this cause based on pure negligent conduct of Rodman as their Question No. 3 assumes. Said Question No. 3 should therefore be eliminated.

(4) Rodman's petition states the fourth and last question as follows:

> 4. Whether, if either of such actions may be implied the limitations periods of such Securities Acts should be applied and not the limitations period of the forum state?

Respondents believe that Question No. 4 is spurious in the context of this cause as amplified in the argument portion of this brief.

STATEMENT OF THE CASE

As Rodman's petition acknowledges, plaintiffs' claim against Rodman & Renshaw, the brokerage firm, is based primarily on the admitted and uncontested fraudulent stock manipulation activities of Rodman's employe, Harris Nagorsky, in the course of his employment as a customer's representative with the firm.

At the alleged beginning of the conspiracy to manipulate in July of 1965, Nagorsky was employed in that capacity by Rodman. The record has shown and is not disputed that Nagorsky remained in the employment of Rodman until sometime in the first or second weeks of October of that year. Soon thereafter Nagorsky obtained employment with another Chicago brokerage firm, First Hanover Corporation and continued his manipulation activities with that firm, also a defendant in this cause, into the year 1966. Thus, Nagorsky's activities were hardly limited to "only three weeks" as mis-stated in Rodman's petition.

Respondents also challenge Rodman's statement on page three of the petition that the bulk of the facts alleged in the detailed account of the manipulation in respondents' amended complaint did not involve them or other brokerage house defendants. To the contrary, the heart of the allegations centered around the activities of various customers' representatives including Harris Nagorsky who were conducting the manipulation in the course of their employment and through the facilities of their respective brokerage firms. The conduct of these individual manipulators was the conduct of their respective firms and a

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source of earnings at least in the form of commissions for those firms.

REASONS FOR GRANTING THE WRIT

Respondents disagree with each and every reason cited by petitioner as grounds for granting the Writ of Certiorari, as will be amplified in the argument.

Overall, and in summary, respondents find none of the grounds stated in Rule 19(b) of the rules of this court present in the portion of the decision of the Seventh Circuit offered by Rodman's petition for review.

ARGUMENT

I.

A FRAUDULENT STOCK MANIPULATION IS ACTIONABLE UNDER SECTION 10(b), RULE 10B-5 AS WELL AS SECTION 9 AND WITHIN THE EXTENT OF 10(b) ACTIONS STATED BY THIS COURT. NO CONFLICT EXISTS ON THIS QUESTION IN ANY OF THE CIRCUIT COURTS OF APPEAL.

To respondents' knowledge, there is not a single decision of any circuit court of appeals in the federal circuits that conflicts with the decision of the Seventh Circuit below that a civil action for damages based on a stock fraud manipulation is actionable under Section 10(b), Rule 10B-5 of the Securities and Exchange Act of 1934. Petitioners have cited none to this court, neither did they cite any in the arguments to the Seventh Circuit and to the district court. The latter was had in late 1969 and early 1970 resulting in the decision *Schaefer, et al.* v. *First National Bank of Lincolnwood, et al.*, 326 F.Supp. 1186 (Pet's. App. at pp. A-1, A-12).

Neither does the decision below conflict with any decision of this court. In fact, actionability of stock manipulation under Section 10(b) falls squarely within the guidelines announced by this court in related decisions. Furthermore, the question is not unique. Thus, none of the reasons stated in Rule 19(b) apply to make it either necessary or even advisable that this court grant the writ.

This court has stated on a number of occasions that the civil remedial provisions of the Securities Exchange

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Act of 1934 are to be given a broad, non-restrictive and flexible construction to achieve the remedial purposes of the law. In a recent decision, *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 31 L.Ed. 2d 741, 92 S.Ct. 1456 citing *SEC* v. *Capital Gains Research Bureau*, 375 U.S. 180, 186, this court said:

> In the case just cited the Court noted that Congress intended securities legislation enacted for the purpose of avoiding frauds to be construed 'not technically and restrictively, but flexibly to effectuate its remedial purposes'.

In *Superintendent of Insurance* v. *Bankers Life and Casualty Company, et al.*, 404 U.S. 6, 30 L.Ed. 2d 128, 92 S.Ct. 165 (1971), this court emphatically defined the remedial extent of Section 10(b) as including any sale of a security in connection with fraud.

> Section 10(b) outlaws the use 'in connection with the purchase or sale' of any security of' any manipulative or deceptive device or contrivance.
>
> (30 L.Ed. 2d at pp 132, 133)

and further:

> Section 10(b) must be read flexibly, not technically and restrictively. Since there was a 'sale' of a security and since fraud was used 'in connection with' it, there is redress under § 10(b), whatever might be available as a remedy under state law.
>
> (30 L.Ed. 2d at page 134)

The first question in Rodman's petition in pure and simple contradiction of the above seeks to remove from respondents alternatives under the securities acts a remedy that falls within express language of Section 10(b). In short, petitioner argues for the identical restrictions, inflexibility and technical interpretation this court has so plainly disavowed.

The Seventh Circuit, in permitting plaintiffs' claim to stand under Section 10(b) as well as Section 9, has merely followed in addition to the express language of 10(b), Rule 10B-5, this court's guidelines for interpreting the 1934 act and, in particular, the anti-fraud provisions of Section 10(b). Furthermore, it followed its own prior decisions which stand as the law in this circuit and those of other circuits where we know of no dissent. The key words in the decision below on this issue are that remedies under the 1934 act are "cumulative and not mutually exclusive." (Pet's. App. pp A-24, 25). The Seventh Circuit thereby embraced the basic principle of flexibility in interpreting the statute that this court has decreed.

Petitioner contends that by not restricting respondents' claim to Section 9, it has been "stripped" of what it views as its inalienable protection and defense under that statute. For one, petitioner contends that the 1-3 year limitations provisions of Section 9(e) would result in its dismissal from the action. That is an erroneous assumption as petitioner ignores the application of limitations statutes to conspiracy situations. Here, the conspiracy has been established as active well into 1966 and alleged into 1967, all well within a three-year period of the bringing of this action against petitioner.

Neither would other provisions of Section 9(e) confer a special benefit on petitioner. The cost bond is probably trivial in the context of this litigation. The so-called specific rule of damages seems to provide an element that plaintiffs are presently seeking in the lower court; and provision for recovery for attorneys' fees as an element of damages against liable defendants is one respondents welcome and presently seek as an additional

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element of damages in the district court. In short, petitioners' contention that the failure to restrict respondents' claim to Section 9 deprives him of rights and protections is illusory.

The granting of the writ on the first question would merely lead this court into a debate on an issue of whether and how to restrict fraud claims under the 1934 act with the attendant danger of restricting and diluting well-established principles. Those principles need no further affirmance from this court as shown by their universal acceptance in the circuits. There is no reason for certiorari and therefore the writ ought to be denied.

II.

THE OPINION OF THE SEVENTH CIRCUIT ON PLAINTIFFS' IMPLIED RIGHT OF ACTION UNDER SECTION 17 OF THE 1933 ACT WHILE CORRECT IN ITS FACE WAS NOT A DECISION OF THAT COURT SUBJECT TO REVIEW BUT RATHER GOOD, SOUND DICTUM.

The essence of the Seventh Circuit opinion on the question of implied right of action under Section 17 of the 1933 act was that it did not have to decide this question in light of its affirmance of respondents' 10(b) claim. (Pet. App. pp A-26, A-27). Hence, there was no decision on the validity of a Section 17 claim standing alone and language approving the claim in conjunction with Section 10(b) of the 1934 act represents sound dictum.

We say sound because the language is another example of the adherence by the Seventh Circuit to this court's posture of flexibility and non-restrictiveness in the approach to civil remedies for fraud under the securities acts as a whole.

Nevertheless, as there was no decision in the circuit court of appeals, there is nothing for the Supreme Court to review. Certiorari ought to be denied.

III.

THE PRINCIPAL BASIS OF THE CLAIM AGAINST PETITIONER IS FRAUD THOUGH THE CONDUCT OF ITS EMPLOYE MANIPULATOR, HARRIS NAGORSKY, ALTHOUGH NEGLIGENCE IS ALSO A FACTOR. THERE IS NO CONFLICT AMONG THE CIRCUITS OR DISPUTE FROM THE DECISIONS OF THIS COURT THAT FRAUD FORMS THE BASIS OF A 10(b) ACTION AND APPLICATION OF FEDERAL EQUITABLE TOLLING OF LIMITATIONS UNTIL THE TIME OF DISCOVERY.

In Question No. 3 and in Part III, petitioner Rodman mischaracterizes respondents' claim as based upon pure negligence or, in terms of the Seventh Circuit, "negligently facilitating fraud."

True, the element of negligence is present, particularly in respondents' claim that petitioner failed to properly supervise the conduct of its manipulating customer's representative, Harris Nagorsky.

The principal basis, however, of the claim against Rodman is fraud and liability is predicated upon common law respondeat superior and the statutory controlling persons doctrine under Section 20 of the 1934 act (15 U.S.C. §78t). In addition, respondents intend to prove that the principals of Rodman were aware of the Hercules Galion stock manipulation while it was in progress and did nothing at their firm to stop it.

The Seventh Circuit properly characterized the case against Rodman in the following from its opinion: (Pet. App. p. A-32)

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> Clearly the action of Rodman & Renshaw fell within the ambit of equitable tolling. In their original claim for relief the plaintiffs alleged direct participation in the conspiracy to manipulate the price of Hercules stock as well as negligent facilitation. Even as equitable tolling works to prevent the defrauder from taking advantage of his wrongdoing, it also works to prevent the negligent person from taking advantage of his carelessness.

Petitioner's misapprehending approach in Part III of its brief is an attempt to bring it within the April 14, 1975 grant of certiorari in the case of *Hochfelder* v. *Ernst & Ernst*, 503 F.2d 1100 (7th Cir. 1974). There the principal and apparently the only basis of the 10(b) claim against the independent auditor was negligence in failing to properly audit the brokerage firm, First Securities Company, so as to discover the fraud of that firm and its principal. This court granted certiorari on the question of whether such a claim limited to negligence is actionable under 10(b) together with applications of the statute of limitations.

Here there is no dispute, as petitioner apparently concedes, that in a claim based on fraud, the statute of limitations is tolled until the fraud either was or should have been discovered. *Bailey* v. *Glover*, 88 U.S. 342, 22 L.Ed. 636, 638 (1875). Neither do we know of any conflict in the circuits on this point and petitioner has not cited any. Furthermore, there is no dispute in the immediate cause that respondents did not nor could have discovered their claim based on fraudulent manipulation of Hercules Galion stock until the return of the federal criminal indictment in August 1967, 18 months prior to suit against this petitioner.

There being no conflict to resolve or any of the other elements of Rule 19(b) present, there are no grounds for granting the writ and certiorari ought to be denied.

IV.

NO CONFLICT EXISTS AMONG THE CIRCUITS ON THE PRINCIPLE OF FEDERAL COURT BORROWING OF THE LOCAL STATE STATUTE OF LIMITATIONS IN ACTIONS BASED ON SECTION 10(b) AND OTHER REMEDIAL PROVISIONS OF THE SECURITIES ACTS THAT CONTAIN NO SPECIFIC LIMITATION PERIOD. WHILE THIS SYSTEM WORKS WELL, IF UNIFORMITY IS DESIRABLE IT IS BEST ACHIEVED BY LEGISLATIVE RATHER THAN JUDICIAL FUNCTION.

Petitioners' last ground for certiorari is a request that this court review the well-established practice and law among the circuits of adopting state statutes of limitations in 10(b) actions. This is apparently an appeal to this court's powers of supervision with the implied suggestion that the law among the circuits is in hopeless confusion on the point.

To the contrary, we know of no conflicting decisions among the circuits on the principle of borrowing the forum state statute of limitations in the absence of a specific federal statute and petitioner has cited none. There is simply no need for this court's supervision in the area. That petitioners have themselves been sued well within the applicable Illinois limitation period does not provide any such need.

If uniformity across the land is desirable on the limitations period and remedial provisions of the securities acts including Section 10(b) of the 1934 act, we suggest that the matter be properly and much more simply handled

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by act of Congress. That Congress, however, has not chosen to amend the law in this respect in the 40 some years since the passage of the securities acts of 1933 and 1934 would indicate reasonable satisfaction with the workings of the system and that there is no problem. In the absence of any need or legal justification and this court's exercise of its supervisory power, we again suggest that certiorari be denied.

CONCLUSION

For all the foregoing reasons, respondents request that the petition of Rodman & Renshaw for a writ of certiorari be denied.

Respectfully submitted,

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The merit of Rodman & Renshaw's position in its Petition for this Court's writ of certiorari is magnified by the Respondents' opposition thereto. Respondents do not attempt to discuss or distinguish any of the cases cited by Petitioner and relied upon by Petitioner to show the inconsistencies and conflicts of the Seventh Circuit opinion with governing authority. Instead Respondents seek to convince this Court that the issues are not as portrayed by Petitioner and hence should not be reviewed. Respondents are egregiously in error.

I.

Respondents first seek to dodge the issue, as to whether the specific limitations of Section 9(e) of the Securities Exchange

Act of 1934 may be evaded by permitting an action to be maintained under Rule 10(b)(5), by asserting that their claim would not be barred by 9(e)'s limitations (Brief pp. 2, 8).

Respondents are not candid in this position. In their brief in the Court of Appeals, they conceded that they had waited more than a year, after learning in August of 1967 of the conspiracy, to file their action. The action was filed in February, 1969, approximately eighteen months *after* Respondents acquired this knowledge, well beyond the one year period permitted by Section 9(e). The Court of Appeals also "found" (Pet. App. p. A-35) "The plaintiffs discovered the existence of the fraud in August, 1967."

In addition, Nagorsky's employment with Rodman had been terminated, ending Rodman's liability for his allegedly fraudulent conduct, in October of 1965, more than three years prior to the filing of the action.

On these facts, the action for market manipulation on a national exchange under Section 9(a)(2) would be time barred under Section 9(e). The only reason for resorting to the Rule 10(b)(5) claim is to avoid that bar.

II.

Respondents urge (Brief, p. 9) that the Court of Appeals did not decide whether or not a right of action may be implied under Section 17 of the Securities Act of 1933. The language of the opinion permitting Petitioners to maintain the action is described as "sound dictum."

The effect of the Court of Appeals decision was and is to permit Petitioners to maintain the present action under Section 17. The refusal of the Court of Appeals to rule has the effect of a refusal to grant Rodman's motion to strike this claim. This refusal is hardly dictum. Negatively, the Court has ruled. It has ruled in a manner inconsistent with the precedent cited, precedent to which Respondents have not seen fit to respond.

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III.

Respondents urge (Brief, pp. 6-8) that this Court's holdings in *Affiliated Ute Citizens* v. *United States*, 406 U. S. 128 (1972) and *Superintendant of Insurance* v. *Bankers Life and Casualty Company*, 404 U. S. 6 (1971), permitting an expansive construction of the Securities Acts, somehow justify the failure of the Court of Appeals in the present case to construe the 1934 Act at all.

The Court of Appeals, in reference to the Securities Act aspects of the use, simply ignored the rules of construction urged by Rodman there and in the present petition for certiorari. Anomalously, the Court applied these rules in determining that Respondents' claim could not be asserted under the Sherman Act. These rules emphasize that a particular remedy governs over a remedy granted by general language in the same or another statute. Respondents ignore these basic canons in their present brief, canons bearing this Court's imprimatur as well as those of various circuit courts, and yet Respondents solemnly assure this Court that the Court of Appeals' decision does not conflict with any decisions of this Court or any Court of Appeals.

The rule of "liberal" construction is simply not a license to avoid construction. The remedial purpose of Congress, invoked as the touchstone for the "flexibility" urged, is not served by ignoring Congressional intent expressly manifested in the limitations periods and other incidents of the Section 9 remedy.

IV.

The argument of Respondents on pages 10-12 of their Brief quarrels with Rodman's position that the issue of tolling in the present case is the same as that involved in *Hochfelder* v. *Ernst & Ernst*, 503 F. 2d 1100 (7th Cir. 1974) upon which this Court has granted certiorari on April 14, 1975, docketed here as No. 74-1042.

Here the Court of Appeals did, as Rodman stated in its Petition, permit the statute to be tolled as to it as one who "negligently facilitate(d) the fraud" (Pet. App. pp. A31, 32). The Court did also state, as Respondents now point out, that there was language in "their original claim for relief" alleging "direct participation in the conspiracy to manipulate the price of Hercules stock as well as negligent facilitation" (Pet. App. p. A32). This charge of direct participation was not repeated in the amended claim which was before the District Court at the time of Rodman's dismissal and so was not properly before the Court of Appeals. In deference to the Court of Appeals, it does not appear that its decision was based upon any charge of direct participation in the fraud, but was explicitly and repeatedly related to the charge of negligence which facilitated the fraud.

Respondents, either inadvertently or deliberately, refuse to recognize that the tolling issue is as stated by Petitioner. Their purblindness as to this issue precludes their appreciation that conflict does exist in the current holdings of the Seventh Circuit on this point and the judicial refusals to toll limitations as to those only charged vicariously with fraud relied upon in the Petition. For purposes of Rule 19, a conflict may exist either as to cases of ancient or recent vintage. Here the conflict exists as to both.

Finally, Respondents claim (Brief, p. 11) that Rodman concedes that the statute of limitations is tolled generally, as to claims based on fraud, until the fraud is or should be discovered. Petitioner not only disclaims such a concession, but can only marvel at the disingenuousness with which Respondents assert it as Petitioner's position. The whole thrust of Petitioner's argument with reference to *Bailey* v. *Glover*, 88 U. S. 342 (1875), its forebears and its progeny, is that its tolling doctrine applies *only* to those committing the fraud.

For the foregoing reasons and for the reasons stated in the Petition filed herein, this Court's writ should issue to the

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Seventh Circuit Court of Appeals and its decision reviewed and rectified.

Respectfully submitted,

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